No. 89-1574

IN THE

Supreme Court of the United States

OCTOBER TERM, 1989

GENERAL MOTORS CORPORATION,
GENERAL MOTORS ACCEPTANCE CORPORATION, and
GMAC LEASING CORPORATION,

Petitioners,

v.

DEPARTMENT OF REVENUE,
STATE OF ALABAMA,

Respondent.

PETITIONERS' REPLY TO BRIEF IN OPPOSITION

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While petitioners strongly disagree with numerous points raised by respondent, they feel particularly compelled to address two fundamental points.

I. The Discrimination Resulting from Alabama's Franchise Tax Impermissibly Burdens Interstate Commerce.

Respondent asserts that Alabama's franchise tax does not discriminate against interstate commerce because the tax does not favor "intrastate economic activity over interstate economic activity." Respondent's Brief in Opp., 10-14. Respondent's position is not sound.

It is true that some foreign corporations (like domestic corporations) may conduct business exclusively within Alabama, rather than across state lines. (A Delaware corporation that conducts all of its business in Alabama is nevertheless subject to the franchise tax on foreign corporations.) However, other foreign corporations, such as petitioners, are engaged in interstate commerce in the several states, including Alabama. (R. 161, 172; 177, 189; 194, 212.)

Corporations that are chartered outside Alabama and are engaged in business within the State as well as elsewhere, incur a higher cost for the privilege of carrying on business in Alabama than competing domestic corporations due to the disproportionately heavy franchise tax burden foreign corporations bear under the Alabama taxing scheme. In other words, because Alabama's franchise tax, on its face and in effect, places all foreign corporations engaged in business in Alabama at a distinct competitive disadvantage relative to their domestic counterparts engaged in the same business activity locally, the tax necessarily discriminates against those foreign corporations, such as petitioners, that carry on business in Alabama through the medium of interstate commerce. The Alabama scheme thus provides an impermissible advantage to local businesses vis-a-vis their interstate competitors, in violation of the Commerce Clause. *Halliburton Oil Well Cementing Co.* v. *Reily*, 373 U.S. 64 (1963).

Respondent claims that such discrimination as there is under Alabama's franchise tax results merely from the decision by corporations to "elect to have their corporate fictions governed by one set of rules or another." Respondent's Brief in Opp., 14. That may

be true, but it does not justify the imposition of an impermissible burden on those corporations that choose not to domesticate in Alabama. Stated differently, Alabama's franchise tax cannot escape Commerce Clause scrutiny simply because foreign corporations doing business there may relocate their corporate charter to Alabama in order to avoid the higher tax burden imposed on them. This Court has struck down such parochial legislation in the past. *See Best & Co.* v. *Maxwell*, 311 U.S. 454 (1940); *Halliburton Oil Well Cementing Co.* v. *Reily*, *supra*.

The very purpose of the Commerce Clause is to guarantee free, uninhibited trade among the states. That purpose is totally frustrated by barriers such as those erected by Alabama, that penalize an out-of-state corporation for not electing to domesticate in a state if it wishes to do business there. *See Metropolitan Life Ins. Co.* v. *Ward*, 470 U.S. 869, 881 (1985) (Alabama tax on foreign insurance companies held violative of Equal Protection Clause; Commerce Clause concerns noted). Alabama's taxing scheme clearly violates the Commerce Clause and cannot be allowed to stand.

II. Petitioners Have Established that the Alabama Taxing Scheme Violates the Equal Protection Clause.

Respondent asserts that the decision below properly rejected petitioners' Equal Protection claim because petitioners failed to prove that the discrimination against foreign corporations was unrelated to a legitimate state purpose. Respondent's Brief in Opp., 15-20.

The only purpose stated by the Alabama legislature in adopting the current franchise tax scheme was that it was intended as a response to this Court's decision

in *Southern Railway Co.* v. *Greene*, 216 U.S. 400 (1910), and was designed to *avoid* discrimination between foreign and domestic corporations doing business in Alabama. The Alabama Supreme Court fully recognized this fact. (Pet. App. 33a-34a.) However, where the sole purpose for a taxing scheme is to avoid discrimination, but in fact it produces the very discrimination it was designed to avoid, the original purpose clearly cannot currently provide the requisite legitimacy for the tax.

The only purpose offered by the State below as a justification for the discrimination between foreign and domestic corporations was "offsetting possible difficulties of enforcing the franchise tax against foreign corporations." (Pet. App. 43a.) Assuming it is appropriate to consider an alternative purpose not attributable to the Alabama legislature, petitioners completely negated the legitimacy of that asserted purpose through the testimony of Ernest Broadhead, Chief of the Franchise Tax Division of the Alabama Department of Revenue. Broadhead concluded that, in fact, it was easier to enforce the franchise tax against foreign corporations than against domestic corporations. (R. 625.) It is difficult to imagine a clearer refutation of the legitimacy of the State's proffered purpose. The Court of Civil Appeals relied specifically on Broadhead's testimony in concluding that the challenged classification had "no legitimate state purpose." (Pet. App. 44a.)

In addition, the absence of a rational relationship between the Alabama taxing scheme and the proffered purpose was unequivocally evident from the affidavit of petitioner GMAC Leasing Corporation, to the effect that it paid 11,000 percent more in taxes

for the years 1983-1986 than it would have paid had it been a domestic corporation. (*See* Pet. App. 82a.) Not even respondent suggests that any cost differential that might be incurred in regulating foreign and domestic corporations could approach 11,000 percent.

No doubt recognizing that its reliance on the "difficulty of regulation" purpose might be questionable in light of the foregoing evidence in the record, the Alabama Supreme Court offered up for the first time in its decision below some new purposes that it thought could legitimize the challenged classification. Those purposes were suggested to be "differences in the utilization of state natural resources between foreign and domestic corporations, and differences in the employment of state residents and utilization of state services between foreign and domestic corporations." (Pet. App. 36a.)

Even assuming it is appropriate to consider the legitimacy of purposes offered by *counsel* for the State without any evidence that the legislature itself had considered such purposes, at no time has this Court sanctioned a state court's unilateral introduction of additional "conceivable" purposes that were not even suggested by the State's counsel. If thus allowed to validate the Alabama tax, the decision below may well be viewed as a landmark in Equal Protection jurisprudence.

In any event, nowhere does the Alabama court indicate whether foreign corporations use more or fewer natural resources, employ more or fewer residents, or use more or fewer state services, than their domestic counterparts. It is thus difficult to understand the suggested link between those factors and the

discriminatory Alabama tax. Moreover, the answer to any of those questions, and thus their relevance to the issue here presented, would seem to turn *exclusively* on the extent of the corporation's *actual presence* in the State, as reflected in the amount of its business activity, and *not on the place where its charter is filed.*

In other words, since the place of incorporation (what respondent calls the "corporate fiction") *by itself* would seem to have *no effect whatsoever* on the extent to which a corporation uses Alabama's natural resources, or employs Alabama residents, or uses Alabama state services (except to the de minimis extent necessary to handle its charter filing), there is *on the face of it* no rational relationship between the challenged classification and the Alabama Supreme Court's suggestions of possible legitimate purposes. It would be totally inappropriate to allow a discriminatory tax such as that here involved to escape an Equal Protection challenge on the ground that the challenging party failed to negate a group of obviously irrational purposes offered up for the first time in the opinion of the State's highest court.

Surely there must be some limits on who can suggest "any conceivable purpose" on behalf of the State, and a requirement of some measure of "colorable validity" to the purposes being suggested, before a failure to negate them can result in a failure to invalidate the tax. If the rule is otherwise, parties challenging discriminatory taxes such as the Alabama franchise tax face a truly insurmountable burden, one that certainly could not have been intended by prior decisions of this Court such as *Lehnhausen* v. *Lake Shore Auto*

Parts Co., 410 U.S. 356 (1973), and the cases there cited.

Conclusion

If, contrary to petitioners' view, it is not yet clear that a taxing scheme like Alabama's violates the Commerce Clause, then it is imperative that this Court grant the writ to resolve the controversy. Otherwise, many other states might well choose to consider the adoption of a scheme similar to Alabama's, in order to place as much of their overall tax burden as possible on foreign corporations in furtherance of their own notions of economic protectionism.

This Court should also grant the writ to clarify the true scope and meaning of the "any conceivable purpose" doctrine as applied in Equal Protection cases.

Respectfully submitted,

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